

VZCZCXYZ0017
OO RUEHWEB

DE RUEHKT #2251/01 2301121
ZNY CCCCC ZZH
O 181121Z AUG 06
FM AMEMBASSY KATHMANDU
TO RUEHC/SECSTATE WASHDC IMMEDIATE 2822
INFO RUEHBJ/AMEMBASSY BEIJING PRIORITY 4676
RUEHLM/AMEMBASSY COLOMBO PRIORITY 4914
RUEHKA/AMEMBASSY DHAKA PRIORITY 0037
RUEHIL/AMEMBASSY ISLAMABAD PRIORITY 2906
RUEHLO/AMEMBASSY LONDON PRIORITY 4314
RUEHNE/AMEMBASSY NEW DELHI PRIORITY 0110
RUEAIIA/CIA WASHDC PRIORITY
RHEHNSC/NSC WASHDC PRIORITY
RHEFDIA/DIA WASHDC PRIORITY
RUEKJCS/SECDEF WASHDC PRIORITY
RHHMUNA/CDR USPACOM HONOLULU HI PRIORITY

C O N F I D E N T I A L KATHMANDU 002251

SIPDIS

NOFORN
SIPDIS

E.O. 12958: DECL: 08/18/2016
TAGS: [PINR](#) [ECON](#) [EFIN](#) [EINV](#) [PTER](#) [NP](#)
SUBJECT: (C/NF) NEPAL'S FINANCIAL SITUATION AND CAPITAL
FLIGHT (C-NE6-01062)

REF: A. SECSTATE 124899

[1](#)B. KATHMANDU 1652

Classified By: Ambassador James F. Moriarty. Reasons 1.4 (b/d).

SUMMARY

[1](#)1. (C) The continuing extortion and intimidation of businesses in Nepal by the Maoists has created a significant problem for foreign- and Nepali-owned businesses in Nepal. Maoist activities against business have continued despite the cease-fire Code of Conduct. This threat has caused many businessmen and industries in Nepal to relocate, or consider relocating, to another country, mainly India. Legal restrictions on movement of capital have forced many businessmen to find creative ways to transfer capital out of Nepal. Businesses have lost faith in the ability of the Government of Nepal (GON) to protect them, and most businesspeople do not believe the GON will be able to address security issues anytime soon. End Summary.

Foreign Investment Under Threat: Businesses Relocating

[1](#)2. (C) Many businesses and industries have been adversely affected by the Maoists, especially since the GON dropped its terrorist designation from the Maoists in May, allowing the Maoists to operate openly and freely throughout the country. Maoist extortion, intimidation and coercion of businesses appears to have increased despite the cease-fire Code of Conduct signed between the Government of Nepal (GON) and the Maoists in May, which bars such activities. Increasing numbers of manufacturing and service industries in Nepal, both domestic- and foreign-owned, have either been forced to close down by the Maoists or chosen to relocate to other countries where the investment atmosphere is better. Although many of the affected industries were initially located in southern and southeastern Nepal (Birgunj and Biratnagar), businesses in Kathmandu and eastern Nepal have also been affected. Industry in western Nepal had been affected extensively earlier in the Maoist insurgency.

[1](#)3. (C) This is a partial list of Maoist-caused closures since the beginning of the current cease-fire in April 2006 (Note:

Point twelve of the 25 point Code of Conduct for the cease-fire states that, "both sides shall create an environment for regular operation of...industrial establishments." End Note.):

-- In early May, the Maoist-affiliated All Nepal Trade Union Federation-Revolutionary (ANTUF-R) began to intensify efforts to enforce unreasonable "standards" for employees and facilities, extort money, and force appointment of local Maoists as permanent employees at most manufacturing and service industries in Nepal.

-- In May, ANTUF-R, supported by Maoist militias, forced dozens of manufacturing industries situated near Birgunj (on the Nepal-India border) to shut down operations indefinitely because the industries could not keep up with Maoist extortion demands.

-- On May 19, ANTUF-R intensified physical violence and extortion, demanding approx. USD 1.3 million in "tax" from Dabur Nepal, a joint India-Nepal venture that manufactures hygiene products and fruit juices, forcing Dabur to close down operations.

-- In late May, ANTUF-R went after dozens of Indian-owned industries in Birgunj, demanding that the businesses fire all Indian employees. Many of the industries decided to close down and transfer operations to India.

-- From May to August, approximately 70 percent of the nearly 250 carpet factories in Nepal shut down due to increasing ANTUF-R activities and demands. Sources stated that, in early 2006, most carpet industries in Nepal were doing "relatively well," but that there had been a significant drop since ANTUF-R activities began in earnest. Most of the

carpet factories that have remained open are no longer producing carpets but only trading in remaining stock.

-- From May to August, a majority of the textile factories in Nepal closed down. Some of these factories closed down due to the termination of Nepali textile quotas in early 2006, but the majority were forced to close because of Maoist pressure. On June 22, nearly 50 textile industries in Birgunj closed indefinitely due to a dispute between management and ANTUF-R. Out of approximately 400 textile factories in Nepal, only five or six currently remain in operation.

-- In late July, The Maoist-affiliated All Nepal Hotel and Restaurant Workers Union (ANHRWU) forced two Indian nationals working at casinos in Kathmandu to quit their jobs.

-- On August 13, ANTUF-R forced an indefinite closure of all tea estates and factories in eastern Nepal. The closure affected 115 tea estates, 40 tea-processing plants, and 40,000 workers and continues to cause a loss of approximately USD 135,000/day.

Capital Flight: Many Informal Methods

14. (C) Anecdotal evidence suggests that capital flight from Nepal is increasing. Numerous sources told Emboff that they have transferred assets and capital out of Nepal, but GON regulations prevent legal transfer of capital. The main method to illegally transfer funds out of Nepal is through "hawala." (Note: Hawala is an informal process whereby money is transferred through family or association networks from country to country, but the money does not actually cross an international border, like an informal banking system with no records. End Note.) There are many hawala lenders in Nepal who transfer money to India, Pakistan, the U.S., the Middle East, and other places. Additionally, some businessmen reported that they simply carried cases full of cash or stashed money in trucks of goods across the porous border between Nepal and India. These two methods are, by far, the most frequently reported methods for transporting capital out

of Nepal.

15. (C) Some of the larger businesses are using legitimate methods in illicit ways to transfer capital out of Nepal, especially to India. Large businesses have reportedly created shell corporations in India or other countries and then placed large orders to import goods from those corporations. When the imported goods arrive, the companies either inflate the bills so they can transfer higher amounts of money to their shell corporation, or bribe import officials in Nepal to doctor the paperwork to make it look like more items were imported. This allows them to transfer large sums of money to their shell corporation in the other country.

16. (C) Another businessman told Emboff that he and his family have taken large amounts of jewelry and precious stones and metals out of the country. They carried the valuables across the border to India and sold them, investing in land or businesses in India. This method of transferring capital appears to be not as widespread as others.

No Faith In the Government

17. (C) Banwari Lal Mittal, Former President of the Nepal Chamber of Commerce, told Emboff that Maoist union activities had paralyzed operations in ninety percent of the factories in the Birgunj and Biratnagar areas. Mittal complained that security was a huge problem for businessmen in Nepal. Maoists have attacked businessmen both in their homes and in their place of business. Mittal claimed there had been no protection provided by the GON against such attacks. Birendra Bahadur Chhetri worried that the Maoists had branded all businessmen as "class enemies" and that the Maoists would continue to "extort and pressure industries until they bow to Maoist demands or leave the country." Chhetri stressed that the Maoists were "not sparing any sector, be it foreign

employment, hotels, tourism, or transportation.

18. (C) One businessman said that "wise businessmen are leaving Nepal immediately and foolish nationalist businessmen are holding out hope for a better business climate in Nepal." Most of the business leaders that Emboff spoke to shared this sentiment. Businessmen did not have faith that the GON would protect them, and did not believe that the GON could stand strong against the Maoists and solve the problems facing the business community. Most businessmen, both Nepali and foreign, had begun to search for ways to transfer their capital out of Nepal and into neighboring India to save their businesses.

Comment

19. (C) Capital flight from Nepal is not an entirely new phenomenon, but continued pressure from the Maoists has caused it to approach a crisis. With the fear by businessmen that Maoists could enter into an interim government soon, businesses are becoming increasingly concerned and looking for a way out, to India or other countries. If this trend continues, the economy of Nepal could plummet further, putting pressure on the GON during this vital time of transition.

110. (C) The GON has not taken effective action to stop Maoist extortion and coercion of businesses in Nepal. It is noteworthy that, despite the cease-fire, the Maoists continue to extort and intimidate businesses with impunity. Fear among businessmen continues to grow, and as more Nepali- and foreign-owned businesses leave Nepal, the pressure will increase on the GON to solve the problems. This could give the Maoists an extra bargaining chip at the negotiation table during peace talks.

MORIARTY